

The Financial Stability Board and its role in the international financial architecture

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Overview

- The evolving international financial architecture – a quick overview
- The G-20 process and the establishment of the FSB
- The FSB post-crisis policy agenda

The international financial architecture (IFA)
consists of **3 interrelated elements** (Crockett 2010)

- the basic economic model that governs cross-border monetary and financial relations
- the institutional structure that exists to manage and, where necessary, adapt these relations; and
- the distribution of decision making authority in international institutions (their ‘governance’)

...and evolved over time

....from a treaty-based and government-led system Post-war Bretton-Woods system
(Padoa-Schioppa and Saccomanni 1994) with

- the IMF setting rules for a managed international monetary system
- The World Bank providing financing for reconstruction and development.
- the GATT establishing a framework for liberalising trade

- **....to a market-led Post-Bretton Woods system in a globalised world**
 - With lesser role of IMF in a market-driven international monetary system
 - Greater role of national central banks and regulatory authorities
 - G7-led process of international cooperation with a network of central bank and supervisory Committees (e.g., Basel Committee 1974, IOSCO, IAIS 1994)

..but did not prevent the recent crisis.

- Lack of coordination of regulatory activities and systemic oversight
- Too “light touch” with too much reliance on market forces
- Lack of legitimacy and effectiveness due to the exclusion of key countries from the process

To address the challenges in a globalised world

- How to build an **efficient and safe global financial system**
- How to ensure a reasonably **level playing field**
- How to promote **safety and soundness** without discouraging **innovation** and **market discipline**
- How to reduce **systemic risk** globally

...reforms of the international financial architecture are needed.

- A global systemic risk regulator?
(Hemerijik, 2010)
- A World Financial Authority?
(Eatwell and Taylor, 1998)
- An international financial regulator>
(Reinhart/Rogoff, 2009)

Politics is the art of the possible

Die Politik ist die Kunst des Möglichen

Otto Von Bismarck, *11 August 1867*

The G20 process and the establishment of the FSB

At the 2009 Pittsburgh Summit the Leaders designated the G-20 as the
“premier forum for international economic cooperation.”

G20

- **Established in 1999 by the G7** as a deliberative (rather than decisional) informal political forum to encourage „the formation of *consensus*“ on international issues, with a mandate to promote international financial stability
- Chair (2008 Brazil, 2009: UK, 2010: South Korea, 2011: France, 2012: Mexico) is part of a **revolving three-member management group** of past, present and designated chairs (“troika”) to ensure continuity : **No seat and no permanent staff**
- Low profile in the past - **became the main forum for reforming the international financial architecture in 2008**
- „Leaders Summits“ in Washington (November 2008), London (April 2009), Pittsburgh (September 2009), Toronto (June 2010), Seoul (November 2010), France (2011)



Establishment of the FSB

- Established in April 2009 by the Leaders of the G20 as successor to the Financial Stability Forum (FSF) with expanded membership, broader mandate and enhanced operating structure to

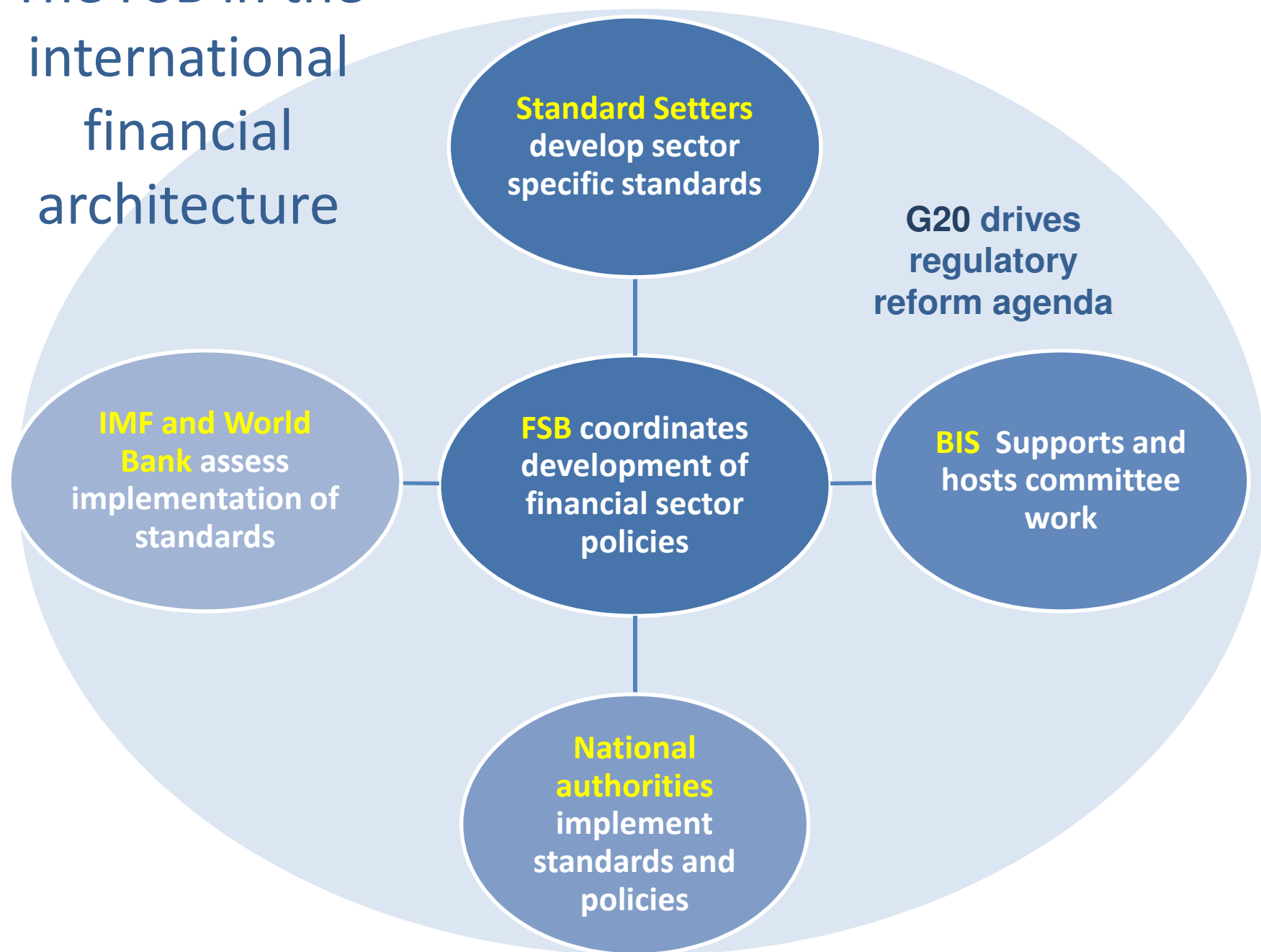
“to coordinate at the international level the work of national financial authorities and international standard setting bodies in order to develop and promote the implementation of effective regulatory, supervisory and other financial sector policies”

FSB Charter, September 2009

...as the **“fourth pillar” of the architecture of global economic governance**, alongside the International Monetary Fund, the World Bank and World Trade Organisation.

Treasury Secretary Timothy Geithner, September 2009

The FSB in the international financial architecture



Membership

- FSB membership falls into 3 categories:
 - member jurisdictions represented by authorities responsible for maintaining financial stability (finance ministries, central banks, supervisory and regulatory authorities)
 - international standard-setting bodies (SSBs), regulatory, supervisory and central bank bodies, and
 - international financial institutions (IFIs).

Member jurisdictions

(central banks, supervisors, finance ministries)

12 existing members:

- Australia (2)
- Canada (3)
- France (3)
- Germany (3)
- Hong Kong (1)
- Italy (3)
- Japan (3)
- Netherlands (2)
- Singapore (1)
- Switzerland (2)
- United Kingdom (3)
- United States (3)

12 new members (2009)

- Argentina (1)
- Brazil (3)
- China (3)
- India (3)
- Indonesia (1)
- Korea (2)
- Mexico (2)
- Russia (3)
- Saudi Arabia
- South Africa (1)
- Spain (2)
- Turkey (1)

Member institutions and standard setters

12 Institutions and standard setters:

- BIS (1)
- European Central Bank (1)
- European Commission (1)
- IMF (2)
- World Bank (2)
- OECD (1)
- Basel Committee (2)
- IAIS (2)
- IOSCO (2)
- IASB (1)
- CGFS (1)
- CPSS (1)

Regional consultative groups

- Creation of six regional consultative groups:
 - Americas
 - Asia
 - the Commonwealth of Independent States
 - Europe
 - Middle East & North Africa, and
 - Sub-Saharan Africa
- Co-chaired by a non-member and an FSB member, both from the region
- Same commitments as FSB members

Governance

Plenary

- Sole decision-making body (consensus)
- Meets at least twice a year

Steering Committee

- To provide operational guidance between Plenary meetings

Chair

- Presides over the Plenary and the Steering Committee
- Appointed by the Plenary for a 3 years term renewable

Secretariat

- Hosted by the BIS in Basel
- Staff seconded from members



Standing Committees

3 Standing Committees established by the Plenary reflecting the three-pronged approach to promoting financial stability:

- SC on **Assessment of Vulnerabilities**
 - to assess risks and vulnerabilities
- SC on **Supervisory and Regulatory Cooperation**
 - to identify supervisory and regulatory actions to address these risks and vulnerabilities
- SC on **Standards Implementation**
 - to assess implementation

Commitments of members

- **Standard-setting bodies** to
 - to report to the FSB on their work to enable the FSB to fulfil its mandates to conduct “joint-strategic reviews” of their policy development \ and to “promote and help coordinate the alignment of the activities of the SBB”
- **International financial institutions** to
 - participate *“in accordance with their respective legal and policy frameworks.”*
- **Member jurisdictions** to
 - pursue the **maintenance of financial stability**
 - maintain the **openness** and **transparency** of the financial sector;
 - **implement international financial standards** (cf. “Compendium of standards”)
 - undergo every 5 years an assessment under the IMF-World Bank **Financial Sector Assessment Program (FSAP)**
 - undergo **periodic peer reviews**
 - **disclose** their degree of adherence

Monitoring implementation

- **G20 Progress Reports on financial reform commitments**
- **FSB Implementation Monitoring Network**
 - drawing on the FSB's peer review processes and on sector-specific implementation monitoring by standard-setters
- **FSB Peer reviews**
 - **thematic :**
 - 2010: compensation, market risk disclosure, mortgage underwriting)
 - 2011: compensation, deposit insurance, tbd
 - **country** (following up on IMF/World Bank FSAPs/ROSCs)
 - 2010: Mexico, Spain, Italy
 - 2011: Australia, Switzerland, Canada
- Establishment of a **Peer Review Council** to review
 - Specific policy measures to reduce moral hazard posed by global SIFIs
 - Ensure consistency of measures and a level playing field
- **Cooperation and information exchange initiative**
 - Confidential policy dialogue and technical assistance
 - Publication of “non-cooperative jurisdictions”?

(Legal) nature of the FSB

- A “soft law institution” “transnational or trans-governmental regulatory network” or manifestation of “global administrative law”?
- The FSB does not
 - have a **legal personality**, neither under international law nor national law
 - have **formal powers** to adopt binding rules and sanction noncompliance and to exercise **oversight** over institutions with the right to obtain non-public market data, etc.
- The FSB Charter is “not intended to create any legal rights or obligations” (Article 16 of the Charter)

Reform priorities

- Reducing moral hazard of systemic institutions (SIFIs)
- Shadow banking
- Reforming over-the counter (OTC) derivatives markets
- Creating a global legal identifier system
- Compensation
- Credit Rating Agencies
- Data gaps
- Consumer finance
- Macro-prudential tools/policy frameworks
- Market integrity and efficiency
- Accounting convergence
- Financial stability issues in emerging market and developing economies (EMDEs)

What makes the FSB work?

- Direct involvement of principal decision makers relevant authorities, bodies with relevant expertise, in the policy making process
- Working “through its members” - joint diagnosis, policy development, Co-ordination and co-operation across policy areas with the Secretariat facilitating the process
- Flexibility and ability to adapt to change

What challenges remain?

- Transparency and accountabilities?
- Legal personality and independence?
- Funding?
- At the Seoul Summit, the G20 asked the FSB to bring forward proposals to “*strengthen its capacity, resources and governance to keep pace with growing demands.*”

„from the politically possible
....to the desirable“

FSB to evolve into a strong cooperative international framework that...

- ...allows for **flexibility and adaptation to change.**
- ...is **transparent and accountable.**
- ...provide **strong incentives for implementation** (“self-enforcing “)